

Impact of Foreign Direct Investment in Indian Capital Market

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ABSTRACT

A well-developed stock market has its impact on the demand side also. It provides investors with an array of assets with varying degree of risk, return and liquidity. This increased choice of assets and the existence of a vibrant stock market provide savers with more liquidity and options, thereby inducing more savings. Increased competition from foreign financial institutions also paves the way for the derivatives' market. Foreign institutional investors have gained a significant role in Indian capital markets. Availability of foreign capital depends on many firm specific factors other than economic development of the country. In this context this paper examines the contribution of foreign institutional investment particularly among companies included in sensitivity index (Sensex) of National Stock Exchange also examined the relationship between foreign institutional investment and firm specific characteristics in terms of ownership structure, financial performance and stock performance. In this paper an effort has been made to develop an understanding of the investment decisions in different group of shares in NSE, and behavior of the FIIs in the Indian equity market of last Five years.

Keywords: Economic, Investments, Returns, Institution

1. INTRODUCTION

Foreign direct investment is a phenomenon resulting from globalization, which involves the integration of the domestic economic system with global markets. It is accomplished through opening up of the local economic sector as well as domestic capital for foreign investors to establish business, within the economy. The portfolio investments by Foreign Institutional Investors, loans by foreign banks and foreign direct investments helped in revoking the gap between needed investment and the real savings of the country. Out of the three mentioned above, India has a special liking for and in fact, holds the maximum foreign funds in the form of Foreign Direct Investments. According to UN report 2012, India emerges as the third most favored investment destination following China and the US. FDI being regarded as the major driving force for the development and growth of country foreign institutional investors have gained a significant role in Indian capital markets. Availability of foreign capital depends on many firm specific factors other than economic development of the country. In this context this paper examines the contribution of foreign institutional investment particularly among companies included in sensitivity index (Sensex) of Bombay Stock Exchange. Also examined is the relationship between foreign institutional investment and firm specific characteristics in terms of ownership structure, financial performance and stock performance. It is observed that foreign investors invested more in companies with a higher volume of shares owned by the general public. The promoters' holdings and the foreign investments are inversely related. Foreign investors choose the companies where family shareholding of promoters is not substantial. Among the financial performance variables the share returns and earnings per share are significant factors influencing their investment decision. Liberalizing foreign direct

investment regulations was important part of India's reforms, driven by the belief that this will increase the total volume of investment in the economy, improve production technology, and increase access to world markets. Foreign Direct Investment (FDI) is one of the most remarkable developments in the past two decades. Foreign Direct Investment (FDI) in a broader sense is any long term investment by an entity who resides outside the host country. A well-developed stock market has its impact on the demand side also. It provides investors with an array of assets with varying degree of risk, return and liquidity. This increased choice of assets and the existence of a vibrant stock market provide savers with more liquidity and options, thereby inducing more savings. Increased competition from foreign financial institutions also paves the way for the derivatives' market foreign entity invests money in the host country for a long period of time. They make an initial investment in the beginning and consequently keep investing according to the needs and requirements of the host country which could be in the form of admittance to better (and cheaper) resources, right of entry to a consumer market or contact to talent specific to the host country - which results in the enrichment of efficiency.

2. REVIEW OF LITERATURE

Abhishek,V.V. (2015). It is an accepted fact that Foreign Direct Investment in any developing/under developed country can play a vital role in its economy; the reason being that there is a gap in the available resources or fund and required resources and fund. It is perceived that FDI fill this gap by pumping required fund and resources and transfer of knowledge and technology as well. This knowledge sharing and technology transfer enhances professional skills, strengthens infrastructure, ensure availability of international brands at doorstep, improve living standards and create employment.

Priyanka, B., & Ekta, K. (2014). Says that regardless of all favorable conditions, India have attracted less FDI inflows when compared to other countries. The study analyzes the problems and challenges that made the country less attractive and made few recommendations to overcome this situation. The study recommend more liberalized policies of FDI in Airports, insurance, media and retail, in addition to implementation of GST, elimination of bureaucratic hurdles and labor law reforms. The paper further states that implementing these recommendations will definitely help to attract more investments in coming years.

De Mello, & Dunning, (1997) The main idea underlying the FDI liberalization policies of many developing countries and the FDI promotion efforts of international donors such as the World Bank and the IMF is the notion that FDI inflows foster economic growth. As FDI is a composite bundle of capital stocks, know-how, and technology, its impact on economic growth is expected to be manifold

3. STATEMENT OF THE PROBLEM

From a global perspective, the relationship between FDI and economic growth, and the stability of this growth, is a central consideration as host countries evaluate the trade-offs associated with foreign entry. This has been considered in the context of longer term performance, stemming from the argument by Romer (1993) that an idea gap has held back growth in emerging markets. If an idea gap has impeded growth, FDI can induce a catch-up process. The most robust evidence on FDI and aggregate growth is found in studies of developing countries. One key feature of today's globalization drive is conscious encouragement of cross-border

investments, especially by Multinational corporations and firms (MNCs). Many countries and continents (especially developing) now see attracting FDI as an important element in their strategy for economic development. This is most probably because FDI is seen as an amalgamation of capital, technology, marketing and management.

4. OBJECTIVES

- To study the trends of flow of FDI.
- To establish the relationship between Foreign Direct Investment and economic growth
- To evaluate the impact of FDI on Indian Stock Market.
- To study is important in the sense that FDI stimulates domestic investment, promotes economic growth and creates employment opportunities.

5. SCOPE OF THE STUDY

FDI investments are considered to be more beneficial for the host country since it directly involves infrastructure development, increase employment opportunities, improved logistic and supply chain system and a lot more to add. It also brings in technology transfer, enhanced governance and management practices. The relationship between FDI, GDP and Market Indices were examined. GDP is taken as the proxy for economic growth. NIFTY and SENSEX were taken as the proxies for stock market movements. Trend in the flow of FDI is studied and its impact on country's economic growth is considered to evaluate the country's current liberalized FDI regime. FDI is also considered as a progressive tool in attaining self-sufficiency of the country as a whole and certain sectors in particular. Considering its massive size of market, sound economic policies and abundant and skilled human resources, India has always been an enhance competency, and preserve intellectual property and shape world's best manufacturing infrastructure in the country.

6. RESEARCH METHODOLOGY

The main source of obtaining necessary data for the study was Secondary data. This study is empirical in nature and hence secondary data is used to conduct the research. The data was collected from the internet by exploring the secondary source available on website. The secondary data constitutes on daily. FDI flows data which was collected from Money control and equity master, the daily returns of SENSEX and NIFTY from BSE and NSE websites respectively, and the trend in FDI from SEBI. Statistical package for social sciences (SPSS) has been used for analyzing the secondary data which have been collected from the following sources. Various bulletins of Reserve Bank of India, Fact sheet of Department of Industrial Policy and Promotion (DIPP) various issues of UNCTAD, Economic Survey- Government of India, and World Bank Reports. The data used in this study have been collected for the time period of 2013 to 2017. In a limited and phased manner market forces were allowed to govern the foreign direct investment flows during this period. Hence this period is selected.

ANALYSIS AND INTERPRETATION**TREND OF FDI, GDP, NIFTY AND SENSEX**

YEAR	FDI (US\$ MILLION)	GDP (US\$ MILLION)	NIFTY (US\$ MILLION)	SENSEX (US\$ MILLION)
2013	28199.45	1936088	6009.51	21170.68
2014	34582.1	2054941	7967.34	27499.42
2015	44208.02	2219669	7983.79	26117.54
2016	45325.85	2359888	8200.55	28145.68
2017	47485.25	2514829	9325.59	29425.25

Source: compiled & computed from the various issues of RBI Bulletin, UNCTAD

TABLE NO 1

By applying the 2tailed Karl Pearson correlation on FDI investment and BSE sensex, the following table emerged

DESCRIPTIVE STATISTICS

	N	MIN	MAX	MEAN	STD DEV
BSE Sensex Average	24	1.0911	2.0249	1.70733	2.2121
		200000	75000	9625000	8.19728
		00E4	000E4	00E4	05823E3
Net FDI (crores)	24	6986.1	32668	1.205E4	9845.2902
Valid N (list)	24				

TABLE NO 2**CORRELATIONS**

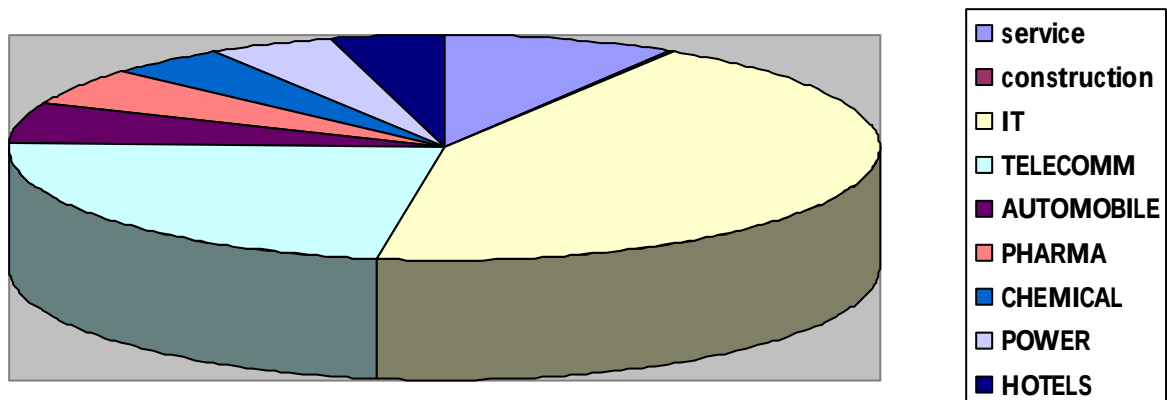
		BSE SENSEX AVERAGES	NET FDI INVESTMENT (CRORES)
BSE Sensex Averages	Pearson correlation	1	.195
	Sig (2 tailed)		.362
	N	24	24
Net FDI Investment (crores)	Pearson correlation	.0195	1
	Sig (2 tailed)	.0362	
	N	24	24

From the above results, it is found that the correlation between Net FII investment and SENSEX is .195. This shows that there is a relationship between NET FDI and SENSEX there is an impact on FDI investment on the fluctuation of SENSEX. This positive correlation establish the fact that the FDI flows are an important driver of Indian Capital market performance and hence have a positive impact on country economic development.

SECTOR WISE FDI INFLOWS

RANK	SECTOR	2016-2017	% INFLOW
1	Service sector	1032	8.49
2	Construction sector	62	0.510
3	Information technology	5288	43.51
4	Telecommunication	2787	22.93
5	Automobile	729	5.99
6	Pharmaceuticals	641	5.27
7	Chemicals	532	4.37
8	Power	559	4.599
9	Hotels	523	4.30

Source: DIPP Fact Sheet on FDI

TABLE NO 3**FIG 1**

Taking a major share of the pie, the computer software industry emerged as one of the rapidly growing sectors of Indian economy. Notable FDI Inflows have been found in computer Software and Hardware Industry from the year 2016-17. The key factors that augmented the FDI inflows to computer software and hardware in India were identified as Software Technology Parks, regulatory reforms by the Indian government, the growing Indian market and availability of skilled workforce. The increase in FDI inflows is due to government driving forward reforms in IT and electronics sector through initiatives like Make in India and by creating favorable policies. The government is targeting zero imports by 2020 and so has embarked on several initiatives to promote manufacturing in the country.

7. LIMITATION OF THE STUDY

The study is general. It is mainly based on the data available in various websites and other secondary sources. The inference made is purely from the past year performance. The time available is limited and subject is very vast. Sufficient time is not available to conduct an in-depth study.

8. FINDINGS OF THE STUDY

The findings of this study will be significant to both academicians and policymakers in the following way; first, it will add to the knowledge of the researchers in this field of study and secondly, it will serve as a guide to both policy makers and academicians. The results would encourage policy makers to design and to follow the pro-FDI policies in developed, developing and the least developed countries. The results would also provide strong evidence to policymakers to work for a better institutional quality for growth and development. There is strong positive correlation between FDI and GDP growth of the country. Thus after analyzing the statistical data it can be concluded that GDP of the country and stock movement were dependent to a greater extent on the FDI inflows into the country.

9. SUGGESTIONS

Empirical results reveal a direct proportional relationship between foreign direct investment and Capital market growth. These findings imply that FDI promotes capital market and suggest that the Indian government embrace policies that aim to attract more foreign direct investment while micro-managing the same to avoid the negative impacts of FDI on local such as crowding out, use of transfer prices to escape local taxes and contribution to economic leakage through preference of imported inputs to local ones the ultimate impact of FDI on growth in recipient economy depends on the scope of efficiency spillovers to domestic firms. Lahiri and Ono (1998) in their investigation on foreign direct investment (FDI), local content requirement and profit taxation in developing countries posited that host countries must strike a balance between costs and benefits of FDI in formulating appropriate policies. The efficiency level of domestic firms must play a role and that a host country should make use of non-tax instruments such as specification on local content of inputs to enhance benefits from FDI.

10. CONCLUSIONS

The aim of Make in India program is to utilize the existing skilled human resources thereby creating surplus employment prospects and empowering secondary and tertiary sector. The regulations of this policy is made as such to reduce or eliminate the existing bureaucratic red tape, avoid unwarranted rules and regulations, making the system transparent and Government responsive and accountable attractive destination for foreign investment entities. Many research papers say that FDI have significant impact on capital market but it can be because of their investment, Indian Institutional Investors as well as retail investor many act on their direction of trading and the overall impact will be positive. Hence we cannot directly say the FDI have a significant impact

Make in India is one of the latest developments in Foreign Direct Investment in India. It is formulated to attract more investments from abroad to reinforce Capital market in India. The initiative is intended to adopt innovation; a significant attribute of India's reorganization program is that it has emphasized gradualism and evolutionary changeover rather than hasty streamlining or "shock therapy". This move was adopted since the reforms were introduced in June 1991 in the wake a balance of payments crisis that was certainly severe. Nevertheless, it was not a lengthened calamity with a stretched period of non-performance. The revised FDI policy includes 100 percent through the government approval route, in defense, resulting in access to capital formation and technological enhancement.

FURTHER RESEARCH

FDI brings much needed physical capital, new technology, managerial and marketing talents and expertise, international best practices of doing business as well as increased competition. These resources may have the potential to be diffused into indigenous firms thereby creating more innovation and productivity growth. Encourage industries to grow to make FDI an attractive junction to invest. Allowing foreign investment in more areas and should be encouraged through different patterns. Simplifying procedure and relaxing entry barriers for business activities and providing investors friendly laws and tax systems for foreign investors.

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